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Financial Sustainability of Sacco's in Kenya: Challenges and Opportunities

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Abstract:- Saving and credit cooperative societies have been cited to contribute immensely to economic development, alleviation of poverty and unemployment in the developing and developed nations. Despite this contribution, many Saccos have been faced with challenges which may threaten their sustainability and survival. The study sought to investigate the major challenges that have threatened the sustainability of Saccos in Kiambu County and propose practical solutions that can be adopted by the Saccos to ensure their survival. Guided by a descriptive survey design the study randomly sampled fifty (50) deposit taking Saccos which formed the basis of investigation. Data was collected with the help of a self- administered questionnaire and analyzed using descriptive statistics. The findings of the study established that among the challenges facing the sampled Saccos three featured prominently, which included competition from other financial institutions such as commercial banks, microfinance institutions, insurance companies and pension provident funds. In addition the study identified that majority of the Saccos are struggling with capital inadequacy and poor liquidity management which is fuelled by poor leadership and improper governance structures. To alleviate competition challenges the study recommends that Saccos can adopt aggressive marketing strategies as well as diversifying their sources of funds. To deal with inadequacy of capital and liquidity management challenges, the study recommends that the directors of such Saccos should develop and implement effective internal control system to ensure proper control, monitoring and maintaining proper level of cash flows. Dealing with the challenge of poor leadership and governance the study recommends that the directors should adopt good cooperative governance principles with regard to appointment of the board of directors, remuneration and determining their terms of service. When the government implements these solutions the Sacco sector will spur economic growth and development.

Keywords:- *Sustainability; Capital Inadequacy; Liquidity Management; Leadership; Marketing Strategies.*

I. INTRODUCTION

A. Background of the Study

Savings and credit cooperative societies (SACCOs) are autonomous associations of persons who join together voluntary, pool their resources together with the aim of meeting their common economic, social and cultural needs. The main objective of any SACCO is to encourage and promote a development thrift culture within its members and educate them on how to efficiently and effectively utilize their limited resources for the attainment of the economic needs (USAID, 2006). Originally Sacco's were formed as an alternative source of funding to the poor with the major aim of alleviating poverty through access to financial services among the poor in the society. Thirlwall (1994) as cited by Mwangi (2011) asserts that gaining financial services is a critical step in connecting the poor to a broader economic life which in return improves the quality of life.

The cooperative movement dates back to 1849 with the first cooperative union which was formed in Germany, in Canada a Sacco union was formed in 1901 and over the years the movement has spread to almost all the countries of the world (Ngombe & Mikwamba , 2004). In Africa, Ghana is cited to be the first country to adopt the cooperative movement in 1959 which later spread to many of the African countries including Nigeria, Uganda and Tanzania (Obure & Muturi, 2015). In most of these countries the main objective of the Saccos' was to improve the livelihood of the members through mobilizing deposits and extending credits to the members.

In Kenya the Sacco movement dates back to 1908 according to the Kenya Union of Savings and Credit Cooperatives (KUSCCO, 2006). Over the years, Saccos have experienced tremendous growth in terms of numbers as well as financial capacity. In Kenya, Saccos are divided into two categories, the deposit taking and the non -deposit taking. Both segments mobilize savings from members' with the aim of advancing loans to their members. The deposit taking Saccos' are regulated by the Saccos society regulatory authority (SASRA) while the non-deposit taking Saccos' are under the ministry of industry, trade and cooperatives. Statistics show that Saccos play a key role in any economy. In Kenya In the year 2017, 22,000 Saccos were registered in Kenya, with over fourteen million members, contributing to 62 % of the country's savings and over 30 % of the country's GDP with and an asset base of over one trillion (state department of cooperative report, 2017). This is implies that the Sacco sector constitutes a significant financial potential which can spur the county's economic and social development.

Despite the significant contribution associated with Saccos towards economic development and improvement of the quality of life of the members', Saccos are faced with mired of challenges which can threaten their financial sustainability. USAID (2006) defines sustainability as the ability to maintain, support or endure in the long term. This means that for the Saccos to be financially sustainable they must cover all their transaction costs, maintain a consisted return on equity and consequently function without subsidies (Njoronge, 2018).

B. *Statement of the Problem*

The Sacco sector has proved to contribute greatly towards economic growth and poverty eradication among many low income earners. According to the SASRA (2017) report for the Deposit-Taking (DT) Saccos, members' deposits increasing by 12% to Kshs.305.3 billion in 2017 from Kshs. 272.57 billion in 2016. On the other hand, the gross loans advanced to members also rose by 11.29 % to stand at Kshs. 331.2 billion in 2017 from Kshs. 297.6 billion reported during the year ending 2016. This underscores the DT-SACCOs mandate in the mobilization of members' savings as well as the advancement of credit facilities.

Despite of the high performance in 2017 SASRA (2018) report paints a different picture on the performance of Saccos in Kenya. This report shows that the quality of the loan portfolio has deteriorated with an increase in non-performing loans beyond the minimum levels of 5% and 3% set by WOCCU and SASRA respectively. The Deposit-Taking SACCOs in Kenya, during the year ending 2017 recorded an increase in the ratio of non-performing loans to 6.14% in 2017 as opposed to 5.23% reported in 2016. This was brought about by an increase in non-performing loans from Kshs. 15.57 billion in 2016 to Kshs. 21 billion in 2017 (SASRA, 2018). This is evident that the challenges facing Saccos are a serious concern which calls for a concerted effort to save the segment from the collapse.

C. *Objectives of the Study*

- To assess the challenges affecting the financial sustainability of Sacco's in Kenya
- To propose market driven strategies to curb the challenges threatening the sustainability of Sacco's in Kenya

D. *Significance of the Study*

The study is expected to play a significant role in highlighting the challenges encountered by Saccos in Kenya. This will enable the regulators to establish better regulations so as to minimize the loss of members' savings as well as ensuring sustainability of the businesses. The findings of the study will also help the investors to understand the position of Saccos before deciding to invest in them. And the study will advance literature on the Sacco sector which is relevant for future researchers.

E. *Scope of the Study*

The study focused on assessing the sustainability of Saccos in Kenya, with the aim of assessing the challenges that could threaten the sustainability of Saccos as well as recommending ways in which these challenges can be addressed. The study focused on a sample of 50 deposit taking Saccos within Kiambu County who were randomly selected.

II. THEORETICAL REVIEW

A. *Poverty Reduction Approach*

Financial sustainability refers to the ability of an entity to cover all operational and financial costs from internally generated income (Kinde & Pradhan, 2012). Financial sustainability can be categorized into two categories (Ganka, 2012). The first category is operational financial sustainability which is the ability to cover operational costs regardless of whether they are subsidized or not (welfarists' approach). The welfarists' approach is concerned with the welfare of the members, where the concern of the institution is to reach as many people as possible and empower them economically regardless of whether the institution is profitable or not without being concerned with the source of funding (Muthomi, 2015). The other category is financial self-sufficiency, which is the ability to cover both operating and financing costs from internally generated income (Zerai & Rani, 2012). This falls under the Institutionists' approach, which advocates for financial deepening with the aim of creating sustainable financial intermediation for the poor. This approach is concerned about ensuring that the institution is profitable enough to cater for the financial needs of the institution based on the profitability theory. When Saccos focus too much on poverty reduction they risk being financially unsustainable since commercialization increases sustainability but decreases outreach (Millson, 2013).

III. METHODOLOGY

A. *Research Design*

The purpose of the study was to assess the financial sustainability of Saccos in kenya with the aim of discovering the challenges facing these organizations and identifying potential opportunities to address these challenges. A descriptive survey design was used to guide the study which involved the collection of survey data and analyzing it to obtain detailed conclusions to facilitate achievement of the study objectives (Mugenda and Mugenda, 2006).

B. *Target Population and Sample Size*

The target population for the study was all the deposit taking Saccos in Kiambu County out of which 50 Saccos were randomly selected to form the basis of the study. To avoid bias in the selection which is a major weakness in random sampling (Kothari, 2008) all the Saccos were where written on small pieces of papers, folded and the researcher picked 50 of them ensuring an equal chance for each paper to being picked.

C. Data Collection Instrument and Procedure

Primary data was collected with the help of a questionnaire which had both open and closed questions which focused on four categories of challenges which were selected as the most common challenges experienced by Saccos from the review of literature.

D. Data Analysis

The collected data was cleaned and edited to ensure only relevant information was used in the analysis. The data was analyzed using descriptive statistics and presented inform of tables.

IV. FINDINGS AND INTERPRETATIONS

A. Response rate

Received/not received	Frequency	Percentage
Received	46	92.0
Not received	4	8.0
Total	50	100.0

Table 1:- Response Rate

Out of the total 50 issued questionnaires 4 (8%) were not returned and thus a total of 46 questionnaires were received (92%) and had all the information correctly provided , this represents a response rate of as shown on table 1.

B. Competition

➢ *Extent of Competition*

Opinion	Frequency	Percentage
Yes	**40**	**86.96**
No	**6**	**13.04**
Total	**46**	**100**

Table 2:- Whether Respondents thought that Competition is a Major Challenge

The study to establish whether the respondents thought that competition was a major concern for the Saccos. From the findings it was established that 40 (87%) of the Saccos felt that competition was a major concern on the sustainability of Saccos. While only 13% felt that competition was not a major problem to their sustainability.

➢ *Source of Competition*

Institution	Rank
Commercial Banks	1
Microfinance	2
Insurance companies	3
Pension funds	4

Table 3:- Source of Competition

When asked to rank which category of the institution posed the greatest competition to their Saccos, majority of them ranked commercial banks as the one with the greatest source of competition, followed by microfinance, insurance companies and pension funds respectively.

➢ *Effect of Competition*

When asked about the effect of competition on an open ended question, the responses some indicating that the banks had enough money to meet their customer demands; those with high income level looked down on Saccos and preferred dealing with banks; banks and other financial institutions had better structures and hence attracted more customer and Saccos have not been able to market their products effectively like the commercial banks hence not make customers are aware of their existence especially the new ones.

These findings were cited by other researchers where they concluded that Saccos operate in a very competitive environment where they compete with other players in the financial industry such as commercial banks, microfinance institutions, insurance companies, pension fund providers as well as capital markets (Ngugi, 2017). The commercial banks have been found to pose the greatest threat in competition to the Saccos (Kagonia, 2017) due to the banks having strong financial muscles as well as clear operating policies compared to Saccos. This challenge has been accelerated by the Central bank of Kenya capping interest rates charged by commercial banks to 13.5% which is closer to the interest rates charged by the Saccos' hence heightening the level of competition. This has had the effect of pushing customers from borrowing from Saccos due to their stringent lending terms (Miriti, 2014)

C. Capital Adequacy and Liquidity Management Challenges

Question	%Positive response (Yes)	%Negative response (No)
Do you lack enough capital to meet customer demands	**75%**	**25%**
Does your Sacco have enough cash to give credit as and when they need it	**34%**	**66%**

Table 4:- Capital Adequacy and Liquidity Management

When asked whether they lacked enough capital to meet customer demands, majority (75%) of the respondents expression their opinion that lack of capital was one of the most common challenges facing them and which has hindered their growth due to inability to meet customer expectations (65%). Said (2013) alludes that capital adequacy is a major component of the success of any organization, this is because when Sacco has adequate capital base it has the capability of shielding members deposits as well as creditors against losses (Saidi, 2013). The findings show that the selected Saccos failed (66%) to provide credit to their customers as and when needed. A Sacco with good asset quality, strong earnings and sufficient capital may fail if it does not maintain adequate liquidity. The Sacco business thrives on trust and confidence of the depositors and investors (Odhiambo, 2012) as quoted by Githaka et al, 2017. Good liquidity management strategies enable an entity to pay the short term obligations when they fall due hence eliciting the trust and confidence of the members who are the major source of funding for Saccos. This has contributed to a shortage in the capital base of the institutions hence hindering their abilities to meet the financial demands of their customers and constraining their growth and survival. Saccos' focus on giving credit to low income earners in the form of groups and individuals (Nkuru, 2015). As a result of focusing on low income earners they are constrained by the low capital contribution and capability hence the need for good liquidity management strategies. Many Saccos have been found to lack proper liquidity monitoring systems (Makori, Munene & Muturi, 2013). As a result they are faced with a shortage of finances to lend to customers. Poor liquidity management has been attributed to constrained growth in the Sacco sector (Wanjala, 2015).

D. Leadership and governance

Question	Positive Response (Yes)	Negative Response (No)
The chairman is the CEO of the Sacco	**67%**	**33%**
The Sacco members participate in board appointment	**42%**	**58%**

Table 5:- Leadership and Governance Challenge

The study found out that the challenge of duality of the chairman of the board and the CEO was prominent (67%) among the sampled Saccos. The major challenge of the management of Saccos is the organizational structure of many of the Saccos. Majority of the board members are selected from the circle of friends or family members without the concern of their competence in the management of the Saccos. Scholars assert that leaders following good corporate governance principles make decisions that are in line with all the stakeholders. Poor governance has also stemmed from un informed cooperative members who are manipulated by few individuals in electing corporative officials (Baka, 2013). This result to Saccos being managed s private or family owned entities hence affecting their growth. As a result of poor leadership Saccos have been faced with the challenge of mismanagement and misappropriation of resources threatening their sustainability.

The findings also show that majority (58%) of the Sacco members do not take part in the appointment of the board members. Poor members' participation has also impacted the governance of Saccos. People participation in their own development is central for good , effective and efficient governance of Saccos (Baka, 20130. Such participation need to be fair and free of intimidation, duress or undue influence. All processes, decisions and relevant information should be conducted in a transparent manner and should be accessible to all concerned.

V. STRATEGIES TO OVERCOME CHALLENGES FACING SACCO SUSTAINABILITY IN KENYA

A. Adoption of Competitive Marketing Strategies

In a competitive business environment no sales can be realized without proper marketing. Through aggressive marketing Saccos will be able to recruit more members, retain existing ones and better position their brands, products and services competitively to the general public.. Saccos should invest into roust marketing drives where the marketing department will considered as a real engine for driving growth strategy instead of being treated as a cost centre.

Ngugi (2017) asserts that adoption of competitive strategies such as cost leadership and differentiation has a positive impact on sustainability of Saccos. To succeed the Saccos should tailor their product in accordance with the target market so as to differentiate products targetimg the low income earners from those targeting higher income categories and adopt differing terms for each category.

Saccos should also diversify their products so as to increase the depth as well as width of outreach. This can be done by developing tailor made products for each category of members. In addition the cooperative societies can diversify into un-tapped markets such as the diaspora market. A Report by the central bank of Kenya shows that Kenyans working abroad sent home Ksh 3.8 Billion in the year 2018. To tap into this market a diaspora strategy that can offer these Kenyans an opportunity to save and invest through Saccos will tap into such remittances with an impact of increasing net earnings and reducing competition from other financial institutions.

B. Strong Internal Controls to Improve Capital Adequacy and Liquidity Management Challenges

To solve the challenge of low capital base, the industry players in the financial sector should advocate for a trading platform for Saccos where members can freely buy shares in their preferred Saccos which will increase the potential for more funds and growth. In addition, Saccos can find cheaper sources of funding to lessen the funding burden from low income level members. They can create a pool of funds where Saccos can borrow at lower interest rate to curb the level of competition from commercial banks.

Attracting capital is important for the Saccos but also management of such funds is key to the success of these institutions. Saccos should also develop and implement proper internal control system that is able to assess, monitor and evaluate and minimize liquidity risk. This will require the establishment of appropriate policies and processes to manage cash flows.

In addition Saccos can enhance their sources of funds by introducing donor funding in form of venture capital where they can even tap and benefit from the strong business management skills and experience from the owners of the money.

C. Good Corporate Governance Principles for Leadership and Governance Challenges

Nyoro and Ngugi (2013) cited managerial in competences as a key driver to Saccos failure. This is because with proper leadership and governance in place, Saccos are bound to make effective and efficient decisions which can lead to better performance of Saccos. With the right people in leadership Saccos can have strong loan processing system that would see them avoid or reduce the level of bad debts. Such systems may include credit rationing for customers and doing due diligence before granting customers loans. Good corporate governance principles will see the Saccos have strong internal controls that would promote membership growth as well as enhance outreach.

VI. CONCLUSION

Based on the above findings the study established that the Sacco sector in Kenya has immense potential to spur sustainable economic growth and development, but the sector is struggling with challenges which if not checked may threaten their sustainability. This can only be achieved if the government in its regulatory role takes up the initiative of supporting the sector in an effort to alleviate all the challenges identified in this study and implement the suggested practical solutions. This will not only spur economic growth but also will improve the livelihood of the millions of Kenyans who depend either directly or indirectly on Saccos for their livelihood.

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